BUDGET MESSAGE

City Administrator's Budget Message

INTRODUCTION

In accordance with Section of 604 the City Charter we are pleased to present the Fiscal Year 2013 Recommended Operating and Capital Budget. This is the second year of the two-year financial plan approved by City Council in June 2011 and, as such, this document represents an addendum to that plan.

In line with the purpose of preparing a two-year plan, the overall approach during this budget process was to minimize changes to programs, services, staffing, and the overall budget. As a result, the recommended expenses represent a continuation of the same levels of staffing and services with relatively small changes.

There have been some significant changes, however, on the revenue side of the ledger, in particular with the General Fund. When the two-year financial plan was presented last year, we projected a $2.7 million deficit for fiscal year 2013. We have been able to close that gap, primarily due to unexpected strong growth in sales tax and transient occupancy tax revenues. We are also proposing the use of several one-time funding sources totaling $879,908. Even with the use of these one-time monies, the proposed budget is balanced without the use of General Fund reserves.

For the first time in three years the General Fund will be balanced without the need for salary and benefit concessions from City employees. The concessions negotiated with labor groups were critical in managing through the last three years when the General Fund faced significant deficits due to declining revenues.

It appears that the worst of the recession is behind us and the local economy is well into recovery. However, there is still work ahead of us as we deal with a remaining ongoing structural deficit. The City also faces several long-term financial challenges, including the funding of major infrastructure needs, worsened by the elimination of the City's Redevelopment Agency, and the continuing burden caused by high pension costs.

OVERVIEW OF FISCAL YEAR 2013 RECOMMENDED BUDGET

The fiscal year 2013 recommended citywide operating budget totals $252.3 million and a total capital program of $19.8 million. The chart below shows the breakdown of the operating budget by fund type.

Fiscal Year 2013 Recommended Budget Summary

	Operating Budget	Capital Program	Total
General Fund	$ 105,748,763	$ 625,000	$ 106,373,763
Enterprise Funds	100,428,284	11,065,328	111,493,612
Special Revenue Funds	29,542,128	5,626,499	35,168,627
Internal Services Funds	16,610,923	2,468,200	19,079,123
Total	$ 252,330,098	$ 19,785,027	$ 272,115,125

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General Fund

The General Fund is the largest individual fund and accounts for most services associated with municipal government, including parks, recreation, library, police, fire, building and planning services. The General Fund is primarily funded from general tax revenues such as sales, transient occupancy, and property tax revenues.

The fiscal year 2013 recommended budget consists of a $105.8 million operating budget, which is $1.2 million below the originally proposed financial plan. Overall, this is due to lower than projected pension costs and to the elimination of the Redevelopment Agency, both of which are discussed in more detail below.

The capital program totals $625,000 and includes 3 projects: the Mesa Lane steps renovation, design of the Kids World renovation project, and installation of police vehicle video cameras, which are also partly being funded from Asset Forfeiture revenues.

Enterprise Funds

Enterprise funds include the Airport, Water, Wastewater, Golf, Downtown Parking, Solid Waste, and Waterfront Funds. These funds are funded primarily from fees and other user charges.

The operating budgets for all enterprise funds total $100.4 million, representing 39.8% of the citywide total. At $30.3 million, the Water Fund is the largest of all enterprise funds and the second largest fund in the City.

The recommended capital program for all enterprise funds totals $11.1 million. This is consistent with the nature of these operations, which require large capital reinvestment.

Special Revenue Funds

Special revenue funds are used to account for restricted revenues. Examples of these funds include: the Community Development Block Grant Fund, in which federal funds are used to provide programs targeted to low and moderate income families; the Creeks Restoration and Water Quality Improvement Fund, which is funded from a 2% transient occupancy tax approved by City voters in 2000; and the Transportation Sales Tax Fund, which accounts for a ½ cent sales tax measure approved by County voters to fund improvements to local streets and highways.

The recommended operating budgets of Special Revenue Funds total $29.5 million, and have a recommended capital program totaling $5.6 million. The largest share of capital relates to the Streets Fund at $3.6 million, which uses restricted funds to pay for streets maintenance, repair and replacement.

Internal Service Funds

Internal service funds account for services provided internally to City departments. These services include information systems management, vehicle maintenance, facilities maintenance and risk management. The recommended operating budgets for all internal service funds total $16.6 million. The combined capital program of $2.5 million is divided between the Information Systems Fund for scheduled hardware and software replacements, and the Fleet Management Fund for scheduled vehicle and equipment replacements.

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GENERAL FUND FINANCIAL HIGHLIGHTS

Revenues

After several years of general declines, two of the General Fund's key revenues – sales taxes and transient occupancy taxes – have posted strong gains. The largest General Fund revenue, property taxes, has remained flat over the last few years following many years of very strong growth.

TRANSIENT OCCUPANCY TAXES				
	FY 2012		FY 2013	
Month	Actual and Projected	Growth	Projected/ Actual	Growth
July	$ 1,763,206	12.2%	*$ 1,868,998*	*6.0%*
August	1,697,686	6.7%	*1,799,547*	*6.0%*
September	1,255,217	8.7%	*1,330,530*	*6.0%*
October	1,126,506	6.4%	*1,194,096*	*6.0%*
November	845,583	12.3%	*896,318*	*6.0%*
December	709,979	8.9%	*752,578*	*6.0%*
January	774,725	11.9%	*821,209*	*6.0%*
February	831,021	11.9%	*880,882*	*6.0%*
March	*874,542*	*6.0%*	*927,015*	*6.0%*
April	*1,124,094*	*6.0%*	*1,191,540*	*6.0%*
May	*1,159,325*	*6.0%*	*1,228,885*	*6.0%*
June	*1,340,859*	*6.0%*	*1,421,311*	*6.0%*
TOTALS	***$ 13,502,744***	***8.4%***	***14,312,908***	***6.0%***

Transient occupancy tax (TOT) revenues began their recovery in February 2010. Since that time, TOT revenues have grown in each of 25 months through February 2012, averaging 8.6% growth per month.

Through the first eight months of fiscal year 2012, TOT revenues grew at 9.6%. The lodging industry is predicting continued strong performance through calendar year 2013. Accordingly, we have assumed 6% growth for the remainder of fiscal year 2012 and all of fiscal year 2013.

The accompanying table presents monthly TOT revenues for fiscal year 2012 and 2013. The portions of the table in yellow represents projected revenues starting in March 2012. In fiscal year 2012, TOT revenues are expected to reach $13.5 million, surpassing the previous high reached in fiscal year 2008 before the full impact of the recession. Based on the assumed growth rate of 6%, revenues are estimated at $14.3 million in fiscal year 2013.

Sales Tax revenues have also performed strongly over the last three quarters. The table below shows Sales Tax growth rates for fiscal year 2011 and 2012 by quarter. As shown below, Sales Tax growth has been strong since the 4th quarter of fiscal year 2011 (April –

Sales Taxes by Quarter

	FY 2011		FY 2012		FY 2013	
Quarter	Actual	Growth	Actual	Growth	Projected	Growth
1st Qtr	$ 4,423,839	3.9%	$ 4,797,256	8.4%	*$ 4,989,146*	*4.0%*
2nd Qtr	4,495,481	2.7%	4,931,326	9.7%	*5,128,579*	*4.0%*
3rd Qtr	3,954,515	3.0%	*4,132,468*	*4.5%*	*4,297,767*	*4.0%*
4th Qtr	4,704,205	11.1%	*4,915,894*	*4.5%*	*5,112,530*	*4.0%*
	$ 17,578,040	5.2%	$ 18,776,944	6.8%	$ 19,528,022	4.0%

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June) through the 2nd quarter of 2012 (October – December), averaging 9.7% in those three quarters.

We have projected a 4.5% growth rate for the remaining two quarters of fiscal year 2012 and 4% for all of fiscal year 2013 (highlighted and italicized sections). Although these projections are more conservative than the recent results, there is still considerable uncertainty about the state and national economic recovery, and it is appropriate to be moderate with our projections.

Property tax revenues have been flat over the last two fiscal years. Previously, property tax revenues grew from 7% to 12% between fiscal years 2001 and 2008. Revenues peaked in fiscal year 2009 at $23.2 million and are expected to fall just short of this high at $22.9 million in fiscal year 2012, representing a projected growth of just 0.5% from last fiscal year.

Although the local economy is recovering, the local real estate market is still stagnant. It appears that it could still be several years before real estate values start to show meaningful growth. As such, we have assumed a modest 1% growth for fiscal year 2013, which would raise property tax revenues to $23.1 million, nearly surpassing the peak of fiscal year 2009.

Impacts of the Elimination of the Redevelopment Agency (RDA)

On July 1, 2011, the State's fiscal year 2012 budget contained two companion measures that were designed to exact payments from local redevelopment agencies (RDAs) totaling $1.7 billion statewide. AB1X 26 (the "Dissolution Act") eliminated all RDAs statewide; and AB1X 27 allowed RDAs the ability to continue to exist if they paid the State a portion of their tax increment revenues – effectively a ransom payment to avoid elimination.

These bills were legally challenged and the case was heard by the State Supreme Court last fall. On December 29th, the State Supreme Court found that AB1X 26 (the Dissolution Act) was constitutional, while the companion measure clearly violated Proposition 22. This result was the worst possible outcome, and resulted in the elimination of our RDA February 1st. It also set in motion a complicated and unclear process of stopping all RDA activity and requiring the sale of all the assets of the agency.

Pursuant to AB1X 26, the ongoing commitments of the RDA that are deemed "enforceable obligations" will continue to be funded from a portion of the property tax increment previously allocated to the RDA. The responsibility for carrying out these outstanding obligations will fall to the City acting as the "Successor Agency."

The long-term impacts to capital funding are discussed later in this budget message. However, the elimination of the RDA has created some operating impacts to the General Fund that are reflected in the fiscal year 2013 recommended budget. These include assuming a number of operating expenses that are not considered enforceable obligations, such as certain staff costs, supplies and services, overhead, and central costs allocated from internal service funds.

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The following table provides a listing of the costs that cannot be funded through tax increment revenues and are proposed to be absorbed by the General Fund. These costs total $1,123,000. There may be other costs that the General Fund may have to cover. The enforceable obligations identified by the City are subject to review and approval by an Oversight Committee created pursuant to the legislation, as well as the State Department of Finance and the State Controller's Office. If it is determined that certain commitments do not meet the definition of an enforceable obligation, the General Fund may have to fund them.

Attorney Costs Previously Charged to RDA	$ 104,058
0.50 FTE Housing Staff Absorbed into other programs	83,000
Overfill of RDA Project Planner (One-Time)	150,000
Police Annex Lease Costs	250,000
Ongoing Ground Water Monitoring - Remediation Sites	39,000
Reallocated RDA Overhead	451,077
Position Changes (CD Business Manager)	5,480
Administrative Staff Partly Funded by RDA	40,385
	$ 1,123,000

On the positive side, the elimination of the RDA will result in additional property taxes allocated to the City, as well as other taxing agencies included within the boundaries of the redevelopment agency. According to the existing property tax allocation formula, the City will receive 12.9% of the net property tax revenues previously allocated to the RDA. This translates into an estimated $1,510,961. As a result, the full $1,123,000 in additional costs to the General Fund will be paid from this additional revenue.

Staff proposes to budget the remaining portion of the new property taxes expected for the General Fund of $387,961 as an appropriated reserve in case other costs have to be funded by the General Fund based on the decisions of the Oversight Committee and State agencies as noted above. The costs at risk of being disallowed total $962,070 and include the following:

1. The Restorative Policing Program - $352,070
2. The funding provided to the Metropolitan Transit District for the Downtown Shuttle Program - $300,000
3. RDA Portion of Remediation of LUFT Sites - $250,000
4. Paseo Nuevo property management costs - $60,000

Fiscal Year 2013 Balancing

Staff is proposing the use of $879,908 in one-time monies to balance the fiscal year 2013 budget. Use of these funds in 2013 will allow us to avoid additional service level reductions and continue to assess the economic recovery. It is entirely possible that with continued strong growth in tax revenues above our projections that we can close the existing structural deficit without further ongoing reductions to the organization. During the year, we will closely monitor both revenues and expenditures in order to react to sudden changes in the economy.

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The following are the sources of one-time funds proposed to balance the 2013 General Fund budget:

Residual in 1998/2005 Disaster Funds	$ 332,040
Liability Insurance Program Rebate	183,102
Capital Project Savings	364,766
Total	$ 879,908

The $332,040 remaining balance in storm recovery funds relates to two federally-declared disasters affecting the City of Santa Barbara. Each was a winter storm, one in 1998 and the other in 2005. Both of the disasters have now been fully closed out and audited by the State Controller's Office, and the remaining balance represents the difference between City costs and amounts reimbursed by both FEMA and Cal-EMA.

The Liability Program Rebate represents surplus funds released by the Authority for California Cities Excess Liability, (ACCEL), a risk-sharing joint powers authority the City participates in for its excess liability coverage.

The reserves in the Capital Outlay Fund were accumulated over the last several years from savings on capital projects. These funds will be used to fund $364,766 of the fiscal year 2013 capital program totaling $1,045,000.

Multi-Year Forecast

Each year, we update our multi-year forecast model to help us assess and identify long-term financial trends. Last year, our forecasts indicated the General Fund had a structural deficit of approximately $2.7 million. Fortunately, because of strong revenue growth, the structural deficit has shrunk considerably.

The table below presents our latest forecast through fiscal year 2015. As shown in the table, we expect to end the current fiscal year 2012 with a budget surplus of almost $1.4 million. This is the third year in a row we have been able to avoid the use of reserves even though we were in the midst of a general economic slump.

GENERAL FUND
Multi-Year Financial Forecast

	FY 2012	FY 2013	FY 2014	FY 2015
Revenues	$ 104,542,533	$ 106,008,997	$ 108,820,299	$ 111,283,742
Expenditures				
Operating	102,658,549	105,748,763	108,700,878	110,539,157
Capital	519,005	625,000	1,000,000	1,000,000
Total Expenditures	103,177,554	106,373,763	109,700,878	111,539,157
Surplus (Deficit)	$ 1,364,979	$ (364,766)	$ (880,579)	$ (255,415)

The recommended fiscal year 2013 budget is balanced with the use of $879,908 in one-time monies. This also represents approximately the same level of the remaining

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structural deficit. As shown in the following table, fiscal year 2014, which assumes no one-time funding, demonstrates this continuing deficit.

Some of the key assumptions and factors upon which the multi-year forecast was built include the following:

1. No wage and benefit concessions are assumed or included in fiscal year 2013. This will be the first year since fiscal year 2010 for non-sworn personnel and since fiscal year 2011 for sworn personnel that wage and benefit concessions are not needed to balance the General Fund.

2. For sworn fire and police, their three-year concession agreement included an ongoing salary increase component that effectively begins in fiscal year 2014. The increase is 5.4% for sworn police and 5% for sworn fire personnel.

3. Fiscal years 2014 and 2015 include an assumed 2% salary increase for all non-sworn and miscellaneous employees. This represents the first increase for most of these employees since 2010.

4. Total revenues are assumed to grow an average of 2.5% starting in fiscal year 2014. However, TOT and sales taxes assume growth of 5% and 4%, respectively. We believe these assumptions are reasonable based upon current trends and economic forecasts.

5. Non-salary costs are assumed to be flat in fiscal years 2014 and 2015.

One of the known impacts starting in fiscal year 2014, which is not reflected in the multi-year forecast, relates to a recent decision by the CalPERS pension board to lower the assumed rate of return for its investments.

For many years, CalPERS has used an assumed rate of return of 7.75% when calculating its member agency contribution rates. In March 2012, the CalPERS pension board decided to lower the assumed rate of return to 7.5%. This change will result in increased contribution rates to all agencies in fiscal years 2014 and 2015 of 1 to 3%. At this point, we have been unable to quantify the financial impacts for the City and, specifically, for the General Fund. We will have better information in October 2012 when the contribution rates for fiscal year 2014 are released. In any case, we can expect higher pension costs starting in fiscal year 2014, which will increase the projected deficit in fiscal years 2014 and 2015.

KEY CHANGES TO ORIGINALLY PROPOSED 2013 FINANCIAL PLAN

With the exception of the elimination of the Redevelopment Agency, the proposed fiscal year 2013 budget contains few significant changes. Most of the proposed modifications are the result of updated estimates based on more current information, such as health insurance premiums, pension contribution requirements, salaries based on the latest staffing levels and pay ranges, and workers compensation, liability and property insurance premiums. In addition, costs have been updated for any Council action taken since June 2011 that impacted future costs.

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General Fund Expenditures

The table below presents, by department, the originally proposed budgets contained in the two-year financial plan (adopted in June of 2011), and the adjustments proposed to arrive at the recommended budget.

	General Fund Expenditures		
	As Originally Proposed	Recommended Adjustments	Recommended
Administrative Services	$ 1,728,969	$ (610)	$ 1,728,359
City Administrator's Office	1,987,269	(2,805)	1,984,464
City Attorney's Office	2,041,924	(44,654)	1,997,270
Community Development	10,470,537	(1,117,038)	9,353,499
Finance	4,639,677	7,520	4,647,197
Fire	22,016,368	(224,169)	21,792,199
Library	4,087,947	(49,036)	4,038,911
Mayor and City Council	746,480	(8,787)	737,693
Community Promotions	2,987,053	421,100	3,408,153
Parks & Recreation	13,091,030	57,587	13,148,617
Police	35,946,740	(150,870)	35,795,870
Public Works	7,243,851	(127,320)	7,116,531
Total	$ 106,987,845	$(1,239,082)	$ 105,748,763

The proposed adjustments total $1,239,082. Two factors that impacted all departments were changes in estimated CalPERS premiums, that reduced costs by $449,825; and changes in expected heath insurance rates, that reduced estimated costs by $281,689. This represents combined savings of $731,514.

The reduction in pension costs is the result of lower contribution rates from the estimates provided by CalPERS last year. The rates will be lower for both the fire and police retirement plans and slightly higher for the miscellaneous plan than the CalPERS forecast.

The reduction in health insurance costs resulted from the decision to bid out the City's health insurance business for calendar year 2012. This competitive process resulted in lower premiums than had been anticipated when the two-year plan was prepared in 2011.

Some of the other key recommended adjustments to the original plan are discussed below.

Community Development

The most significant change occurred in the Community Development Department, which almost entirely relates to the elimination of the City's Redevelopment Agency (RDA). Since RDAs are not established to have their own staff, the RDA contracted with the City for the use of Community Development staff that would be dedicated to administering and

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carrying out the activities and projects of the RDA. With the elimination of the RDA, staff and related operating costs have been removed. Some of these costs have been either absorbed or will be funded temporarily by other programs within the Community Development Department. The net reduction to the Community Development Department's costs is approximately $1.1 million.

Community Promotions Including General Governmental Expenses

This category includes funding for community promotions and appropriated reserves. The proposed plan for fiscal year 2013 includes an increase in appropriated reserves of $387,961, which represents the difference between the additional property revenues expected and the additional costs absorbed by the General Fund as a result of the elimination of the RDA.

Community promotions funding has also been increased by $32,659 to reflect amounts paid to Santa Barbara Channels for capital equipment and facilities. These monies are funded from a capital surcharge included on cable bills. When Cox Communications shifted to a State franchise, the City was allowed to include an additional surcharge for capital, which provides funding to the City TV Program and to Santa Barbara Channels. This expense was included in the fiscal year 2012 budget but, due to an oversight, was not included in the second year of the two-year financial plan.

Fire

The Fire Department's budget was lowered by $224,169. All of these savings are a direct result of the lower CalPERS premiums and health insurance costs noted previously. There are no proposed service level changes in the Fire Department.

Police

The Police Department budget was lowered by $150,870, which is the net effect of several adjustments. Retirement costs dropped by $232,236, due to the lower rates set by CalPERS. Costs for health insurance have been reduced by $162,129 to reflect expected lower costs in fiscal year 2013.

The proposed budget includes shifting $118,000 in personnel expenses to grant and special funding sources to partially fund the acquisition of new video cameras for patrol vehicles. The full cost of the video cameras is budgeted at $250,000 in the General Fund capital program, of which $132,000 will be funded from a transfer of reserves from the Police Asset Forfeiture Fund. This shift in costs will not impact staffing or service levels.

The proposed Police budget includes an increase of $250,000 to cover lease costs for the Police Annex building. This expense was previously funded by the City's Redevelopment Agency. Other costs were increased by $111,495 for a net reduction of $150,870.

Public Works

The proposed General Fund portion of the Public Works Department has been reduced by $127,320. This reduction is a result of shifting staff from the General Fund into other funds based upon the actual work these employees perform. This shift generated savings of $50,344.

These savings were partially offset by additional costs in the General Fund of $66,000 for environmental compliance work associated with leaking underground fuel tanks and $30,000 for rental costs for the recently occupied offices at the Mental Health building at

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619 Garden Street. The $66,000 in environmental compliance costs would have been paid by the RDA, but now must be absorbed by the General Fund with the RDA's elimination.

General Fund Revenues

The proposed General Fund revenues have been updated to reflect current receipts and updated estimates. The recommended adjustments for all General Fund revenues total $1,180,462. The schedule below summarizes these changes.

	General Fund Revenues		
	As Originally Proposed	Recommended Adjustments	Recommended
Taxes	$ 65,432,215	$ 3,085,637	$ 68,517,852
Licenses	182,900	26,088	208,988
Fines & Forfeitures	2,931,167	39,137	2,970,304
Use of Money & Property	1,160,462	22,442	1,182,904
Intergovernmental	1,413,724	(213,161)	1,200,563
Fees and Services Charges	9,874,797	(192,294)	9,682,503
Interfund Charges	16,645,562	(2,060,394)	14,585,168
Interfund Transfers	1,130,128	506,193	1,636,321
Other Revenues	4,857,580	(33,186)	4,824,394
Anticpated Revenues	1,200,000	-	1,200,000
Total	$ 104,828,535	$ 1,180,462	$ 106,008,997

Taxes

The $3.1 million increase in the taxes category is due to increases in three taxes: sales taxes, transient occupancy taxes (TOT), and property taxes. As noted previously, both sales tax and TOT revenues have grown significantly in the last year. On a combined basis, our projections for these two revenues have increased by approximately $2 million.

Estimated property tax revenues have been increased by approximately $1.2 million. This increase is a result of the elimination of the City's Redevelopment Agency, not stronger growth in property values. Due to the demise of the RDA, a larger portion of property tax revenues will be allocated to taxing agencies that are within the RDA project area. As one of the largest taxing agencies, the City will receive a share of the tax increment, estimated at $1.5 million. This amount will be offset by a reduction of almost $300,000 due to lower projections based on actual results in fiscal year 2011 and updated current year estimates.

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Intergovernmental

Intergovernmental Revenues have been reduced by $213,161. $200,000 of this loss is due to the elimination of motor vehicle license fees previously paid by the State. In its fiscal year 2012 budget, the State eliminated this local revenue. It was partially offset by additional funding to local agencies for the COPs program, which is accounted for separately in a Police grants fund.

Interfund Charges

Interfund charges have been reduced by $2.1 million. Approximately $1.9 million of this reduction relates to the elimination of the RDA. Included within this revenue were the charges to the RDA by the Community Development Department for staff assigned to the RDA. With the elimination of the RDA, costs and related reimbursements totaling approximately $1.4 million are no longer budgeted. The RDA was also charged for administrative services provided out of the General Fund, which were reimbursed as "overhead" to the General Fund. Since the RDA was eliminated, General Fund overhead revenue was reduced by $451,077.

Interfund Transfers

The increase of $506,193 includes one-time revenues totaling $515,142 used to balance the General Fund that have been budgeted as non-departmental revenues. The $515,142 consists of $332,040 of transfers from closed out storm recovery funds and $183,102 in rebates of liability program premiums paid into the Self-Insurance Fund in previous years. Other transfers were lowered by $8,949 to arrive at the net increase of $506,193.

General Fund Position Changes

The proposed fiscal year 2013 budget includes several changes that have resulted in reduced staffing levels Citywide. The net result is that a total of 11.85 full-time equivalent (FTE) positions are proposed for elimination citywide.

In the General Fund, the fiscal year 2013 recommended budget includes the reduction of 15.36 FTEs as shown in the table below. Of this total, Community Development accounts for 11.91 FTEs of the decline, mostly related to the elimination of the RDA. Positions previously assigned or allocated to the RDA have either been eliminated or shifted to other funds.

GENERAL FUND
Fiscal Year 2013 Position Totals

	Originally Proposed	Increase (Decrease)	Recomm'd
Administrative Services	12.00	0.00	12.00
City Administrator's Office	9.90	0.00	9.90
City Attorney	11.40	(0.10)	11.30
Community Development	72.21	(11.91)	60.30
Finance	33.85	0.00	33.85
Fire	109.00	0.00	109.00
Library	26.45	(0.25)	26.20
Mayor & Council	8.00	0.00	8.00
Parks & Recreation	70.31	0.00	70.31
Police	206.25	(1.75)	204.50
Public Works	49.55	(1.35)	48.20
Total	608.92	(15.36)	593.56

The Police Department is proposing to move 1.75 FTEs out of the General Fund into other funds. This includes shifting one full-time Office Specialist II and 50% of a police officer into the Police Asset Forfeiture Fund. The Office Specialist II position will be funded from ongoing State grant (SB 720) revenues, and the Police Officer will be funded from

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one-time Police Asset Seizure Fund reserves for fiscal year 2013 only. An additional 25% of a police officer will be shifted to the Supplemental Law Enforcement Fund to be funded from additional ongoing grant revenues from the State. These revenues are a partial offset for the taking of motor vehicle license fees by the State as part of their fiscal year 2012 budget. Overall staffing in the Police Department is not impacted by these changes.

The Public Works Department is also recommending shifting positions out of the General Fund to other funds to offset a reduction in engineering revenues. Portions of four positions, totaling 1.5 FTEs, were shifted to the Streets Fund and Downtown Parking Fund. In addition, an additional 0.15 FTE was allocated to the General Fund to provide additional administrative support. The net effect of these changes results in a reduction of 1.35 FTEs.

The Library shifted 20% of a Senior Library Technician to the County Library Fund's Carpinteria Library Program. In the prior year, 20% of the staff position was allocated to the General Fund due to a lack of funding in the County Library Fund. However, additional funds will be provided from the Friends of the Library, which allows the Library to return the staff back to the County Library Fund. In addition, 5% of a Library Systems Technician II was allocated to the County Library to reflect actual work performed between libraries.

Changes to Enterprise Fund Operating Budgets

The proposed fiscal year 2013 budget for enterprise operations reflects changes totaling $1,262,791. As in the General Fund, enterprise operating budgets were impacted by updated CalPERS costs and revised health insurance premiums. Generally, retirement costs have increased slightly while projected health insurance costs are lower.

The table below provides a summary of the operating budgets for each of the enterprise funds, including the recommended changes proposed for fiscal year 2013.

	Enterprise Fund Expenditures - FY 2013		
	As Originally Proposed	Recommended Adjustments	Recommended Budget
Airport	$ 17,610,810	$ (143,754)	$ 17,467,056
Downtown Parking	6,741,879	40,993	6,782,872
Municipal Golf Course	2,061,017	(303,266)	1,757,751
Solid Waste	18,817,359	(352,413)	18,464,946
Wastewater	13,451,188	715,196	14,166,384
Water	31,595,760	(1,305,439)	30,290,321
Waterfront	11,413,062	85,892	11,498,954
Total	$ 101,691,075	$ (1,262,791)	$ 100,428,284

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Airport Fund

Fiscal year 2013 will be the first full year since the August 2011 opening of the new Airline Terminal. With the completion of the new terminal, the overall revenue and expense structure has changed significantly. Airlines will be paying higher rent and landing fees and concessionaires will be generating operating revenues. These revenues are critical funding components to the repayment of bonds sold to finance portions of the terminal.

In the current year, passenger counts are down 7%. In addition, the terminal opened three months later than forecasted. As a result, commercial aviation revenues (landing fees and rent paid by the airlines) and terminal revenues (concessions and payment from rental cars companies) are expected to end the year below budget. In addition, parking revenues have been severely impacted by the construction and the loss of the short term parking lot that is still under construction.

For fiscal year 2013, terminal revenues are budgeted to reflect a full year of occupancy of the new terminal. This is close to what was originally budgeted in fiscal year 2013 as part of the two-year financial plan. Parking revenues, however, will be below original fiscal year 2013 estimates but still higher than fiscal year 2012 based on the expected completion of the short term parking lot. Commercial aviation revenues are expected to increase in fiscal year 2013 based on scheduled airline flights for the summer and other seasonal changes.

Lease revenues generated from the Airport's commercial/industrial properties have been stable over the last few years since virtually all properties are occupied. For fiscal year 2013, revenues are projected to increase slightly based on annual CPI adjustments built into the long-term leases.

The Airport has reduced their costs in total by $143,754. This was accomplished from the elimination of two full-time positions (one to be deleted when vacant), which saved $215,218. In addition, a third position will be reclassified downward, saving $28,610. These savings were offset by increases to budgeted costs in connection with the new terminal, such as $40,000 for additional custodial services and $56,162 for additional hourly salaries needed to staff a checkpoint exit.

Downtown Parking Fund

The Downtown Parking operation has been financially stable the last few years. Revenues from hourly parking, which make up approximately 64% of total revenues, are shown below:

Fiscal Year	Amount
2009	$ 4,317,178
2010	4,381,938
2011	4,327,200
2012 (Estimated)	4,306,512
2013 (Recommended)	4,350,000

All other revenues, including monthly parking fees, assessments from the Parking Benefit Improvement Area (PBIA), and commuter lots have also been stable.

Starting in November 2011, the Downtown Parking staff implemented a new revenue control system at the manned lots, adding the ability to accept credit payments. Currently, 17% of paid transactions are from credit cards, representing 25% of total hourly parking revenues. This added payment option has been well received and is expected to increase in popularity.

Overall costs in the Downtown Parking Fund are essentially the same as originally proposed in the two-year financial plan, increasing by only $40,993.

One of the long-term challenges of the Downtown Parking operation will be the ongoing maintenance of the parking structures. Historically, the City's Redevelopment Agency (RDA) provided substantial financial support for maintenance and major capital improvements to the parking structures. With the dissolution of the RDA, ownership and responsibility for ongoing maintenance of the parking structures will revert to the Downtown Parking Fund. Over time, capital reserves will need to be built up to align with the added maintenance responsibility. Long-term, this will put upward pressure on parking rates.

Golf Fund

Across the nation, both public and private golf courses have faced declining rounds over the last ten years. The City's Municipal Golf Course is no exception.

Over the last two years, Golf staff have evaluated various fee structures and increased marketing efforts in order to attract and retain more golfers. Fortunately, golf play has stabilized recently, helped by the recovering economy and pleasant winter weather. However, the Golf Fund's financial structure continues to be fragile.

The fiscal year 2013 revenue budget assumes rounds will remain at current levels, and proposes moderate fee increases for the two main discounted play periods, Twilight and Super-Twilight, which are currently deeply discounted.

The recommended operating budget is 4.3% below fiscal year 2012 projected expenses, and 14.7% below what was contained in the original two-year financial plan for fiscal year 2013. The deletion of three vacant permanent positions (2.5 FTEs) and backfilling with hourly staff allowed the Golf Fund to reduce the budget by $182,401. In addition, the Golf Course has refinanced all of its outstanding debt in order to spread the debt service requirements over a longer repayment term, thereby lowering its annual payments by $44,202. Other reductions were made, including eliminating their appropriated reserves of $49,061 and deferring an irrigation project of $25,000.

During fiscal year 2013, the Parks and Recreation Director will be leading a comprehensive analysis of the entire golf operation. This analysis will consider all potential options in order to achieve financial stability in the Golf Fund.

Solid Waste Fund

The Solid Waste Fund was recently classified as an enterprise fund. It is the newest enterprise operation, started in response to State law mandating specific diversion levels. Activities have been implemented over the last decade to raise public awareness and manage programs aimed at increasing waste diversion and reducing amounts of solid waste disposed at the Tajiguas landfill.

One of the key responsibilities of Solid Waste staff is managing the collection, disposal and processing of solid waste generated by City residents and businesses, including recyclable materials, greenwaste, and foodscraps. Collection of the waste is handled by a local trash hauler operating pursuant to a local franchise agreement. The trash portion of the waste is disposed of at Tajiguas Landfill, owned and operated by the County of Santa Barbara.

City Administrator's Budget Message

Since 2003, the City has been divided into two separate zones, each representing roughly half of the City. MarBorg Industries services Zone 2 and, until last year, Republic Services serviced Zone 1. MarBorg purchased the local assets and operations of Republic Services in 2011 and has taken over collection services in Zone 1. With the expiration of the Zone 1 franchise agreement in June of 2013, City staff and MarBorg are currently in exclusive negotiations for a new franchise agreement that will likely extend ten years through 2023.

The fiscal year 2013 Solid Waste Fund recommended budget has been adjusted to reflect the expected payment to MarBorg for collection services, as well to reflect up to date revenue and expense trends. As such, the recommended budget is $352,413 lower than the amount contained in the originally proposed plan for fiscal year 2013.

Solid Waste staff has also been working with the County and City of Goleta on the possible development of a waste recovery project that could significantly reduce the amount of trash buried at Tajiguas Landfill. The project as currently proposed includes a Materials Recovery Facility ("MRF") designed to recover recyclable commodities, and an anaerobic digester facility that will convert the organic portion of the waste stream into energy. The project is expected to enter into the environmental review phase by the summer.

Water Fund

The Water Fund is the City's largest enterprise fund, and pays for the operations and infrastructure that provides potable and recycled water to all City residents and businesses. In addition to securing and maintaining water resources, the division is responsible for extracting water from the City's reservoirs and wells, treating the water in accordance with federal safe drinking water regulations, and delivering the water through hundreds of miles of mains and pipes to residents.

The fiscal year 2013 recommended operating budget has been lowered by approximately $1.3 million. Most of the reduction is due to a decrease of $757,716 in the amount budgeted for chemical and landscape supplies based on longer term historical average costs. Other costs were similarly adjusted to better reflect expectations, while some were deferred in order to position the Water Fund to have the funds available for large capital projects planned in the next several years.

A large component of the Water Fund budget is devoted to the maintenance, improvement and replacement of its aging infrastructure. As such, a portion of the fees charged to customers is to ensure adequate revenues are generated to fund not only operating costs, but a large capital program.

Water staff maintains an internal financial plan that looks forward ten years to identify capital needs and operating costs in order to establish a stable rate policy to minimize large rate increases. In this context, the current fiscal year 2012 budget included a 3.5% rate increase. Coupled with an assumed sale of 13,800 acre-feet of water, revenues from metered water sales are expected to end the current fiscal year at $28.7 million. For fiscal year 2013, staff is recommending again a 3.5% across-the-board rate increase, which is expected to generate an additional $1.1 million above fiscal year 2012, for a total of $29.8 million.

The proposed capital program of $3.25 million includes $2.05 million for an annual Water Main Replacement program. All of these projects will be funded from operating revenues with no use of reserves planned. Although the Water Fund had an undesignated reserve balance of slightly over $7 million, these funds are earmarked for several large projects in the next few years.

Wastewater Fund

A major focus of the Wastewater operations continues to be improvement and replacement of capital facilities. Pipeline renewal is a priority of both staff and City Council and, as such, the capital budget is developed each year with a goal of replacing 1% of pipeline each year. There are also other significant capital needs related to the maintenance and renewal of the wastewater treatment plant that must be met.

Over the next five years, the City will be accelerating its pipeline replacement program as a result of a legal settlement reached with Channelkeeper, a local environmental organization. This settlement will require that $900,000 be spent in each of the next five years in addition to the normal annual pipeline replacement program. To fund the additional pipeline replacements, staff is proposing a 10% rate increase in fiscal year 2013. This is comprised of a 6% rate increase to generate the additional $900,000, in addition to a planned 4% rate increase to fund ongoing operations and ongoing capital maintenance and replacement costs.

Wastewater revenues are generally stable. Through nine months of fiscal year 2012, revenues are in line with budgetary expectations. Total projected revenues in fiscal year 2013 are $17.2 million, which will fund $14.2 million in operating costs and a capital program of $2.9 million. Of the $2.9 million, $2.05 million will be spent on pipeline replacement.

For fiscal year 2013, the Wastewater Fund operating budget was increased by a total of $715,196 in relation to the originally proposed plan. This was due primarily to cost increases in three areas. The first was in vehicle replacement costs for vactor trucks used to clean sewer lines. Due to the unreliability of these vehicles and the high cost to maintain them, the replacement cycles have been shortened from 15 to 5 years, increasing the required annual contribution to the Vehicle Replacement Fund by $267,750. The second cost increase relates to the Local Limits Evaluation for the Pretreatment Program, which is necessary to ensure compliance with Federal Clean Water Act regulations. The review and revision of the local limits will result in additional costs estimated at $225,000. Lastly, additional costs totaling $195,000 for engineering services have been budgeted. In part, these costs have previously been included in the capital program; however, because of the complexities of the capital projects being considered, more of the focus of the engineering services will be to develop better concepts, designs, and solutions to address the overall wastewater treatment system requirements.

Wastewater reserves as of June 30, 2011, were below policy levels by $2.3 million. However, a number of capital projects previously planned to be funded from reserves being financed from a State revolving loan. This will reduce the shortfall in reserves to $672,000 by the end of fiscal year 2012.

Given the lack of reserves above policy requirements and the mandated increased funding for pipeline replacement, staff is evaluating options to debt finance several large capital improvement projects, which may include the sale of revenue bonds.

Waterfront Fund

Waterfront revenues come from three primary sources: (1) parking fees, which include visitor parking and annual permits; (2) slip fees paid by slip holders; and (3) leases paid by merchants with buildings in the harbor and wharf. The good weather this fiscal year has generated better than expected revenues in these areas. Through December 31,

City Administrator's Budget Message

2011, revenue was approximately $600,000 higher than last year. Based on this trend, revenues are expected to exceed budget by $260,000.

Proposed fee increases for fiscal year 2013 are as originally proposed in the two-year financial plan adopted in June 2011:

- Slip Fees - Increase of 2%
- Slip Transfer Fees – Increase of $25 per foot except 20-foot slips

Few changes have been made to the recommended budget in relation to the original proposed plan. The operating budget has been increased by just $85,892, half of which relates to an increase in overhead costs stemming from a citywide reallocation of overhead to adjust for the elimination of the City's Redevelopment Agency.

The Waterfront Department continues to make progress on the rebuilding of Marina 1, the largest marina in the harbor. Begun in fiscal year 2009, the first three of eight phases have been completed at a cost of approximately $5 million. The project has been largely funded from a State Department of Boating and Waterways loan. Phase 4 is planned to begin in the winter at a cost of approximately $2.1 million. The remaining four phases are expected to be completed by fiscal year 2017. Staff hopes to secure additional state loan financing for the remaining phases, which are estimated to cost $7.3 million. Beginning next year, debt service costs will increase to $332,000, and by fiscal year 2014 will reach an estimated $462,000.

LONG-TERM CHALLENGES

Funding Infrastructure Capital

The City owns and maintains assets valued at over $1 billion. Many of these assets are included in the enterprise operations such as Water, Wastewater, Airport, and Waterfront. The enterprise operations have established fees and rates designed to finance a large portion of their capital maintenance and replacement costs.

We are also fortunate to have voter-approved tax measures that provide dedicated funding for our streets (1/2 cent sales tax per Measure A) and creeks (2% TOT per Measure B). In addition, the City annually receives federal and state grants to augment our capital programs.

A large portion of City assets, however, do not have dedicated funding sources that enable the City to keep up with their required maintenance, improvement and replacement. These capital assets include parks, sidewalks, buildings (administrative offices, fire stations, and the police headquarters), playgrounds, parking lots, and other infrastructure.

Over the last 40 years, the City Redevelopment Agency (RDA) provided a large source of funding for capital improvements in the downtown and waterfront areas to eliminate blight and improve economic conditions. RDA funds have also been used to build a number of critically needed affordable housing projects. The dissolution of the RDA in February 2012 eliminated a significant source of revenue for the types of capital infrastructure projects that normally fall within the responsibility of the General Fund.

City Administrator's Budget Message

Several years ago, the City Council created the Infrastructure Capital Financing Task Force, made up of community leaders, to develop strategies and recommendations for financing large capital investments. Unfortunately, the conclusion of their effort and final report was followed by the "Great Recession" that delayed serious consideration of the recommendations. As the economy improves, it is important that we again focus our energies to resurrect and update the report from the Infrastructure Task Force and develop a long-term plan for capital infrastructure financing.

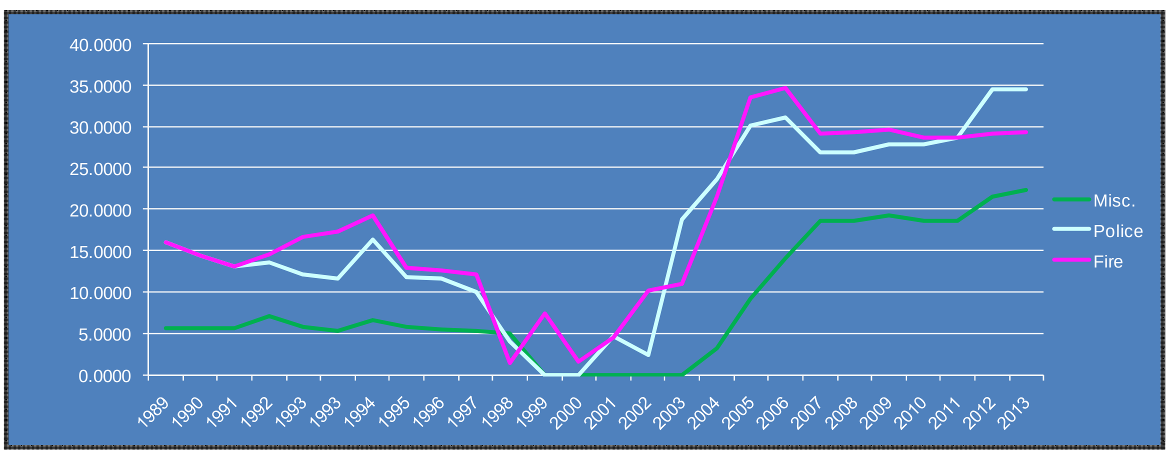
Pension Costs

The City provides retirement benefits to our employees through the California Public Employees Retirement System (CalPERS). CalPERS is the largest public employee retirement system in the country and it provides benefits to State employees and most city and county employees.

CalPERS administers the pension system on behalf of its member agencies, which includes payment of benefits, collecting pension contributions from participating agencies, and investing pension assets. This last function – investing pension plan assets – has a direct effect on what jurisdictions have to contribute to stay in line with the funding plan. When investment performance exceeds expectations, annual contributions from employers go down; and when investment performance is below expectations, contributions must go up to make up the difference.

The chart below illustrates the impacts of the two recessions during the last decade. In fiscal year 2000, following the economic boon of the late 1990s, employer rates were virtually 0%. Since then, they have increased dramatically to a current high of approximately 35% for police, 32% for fire, and 22% for all other employees.

City of Santa Barbara
CalPERS Employer Contribution Rates
Fiscal Year 1989 – Fiscal Year 2013



These significant rate increases are not just due to investment losses; they are also due to benefit enhancements implemented when employer rates were at their lowest. Unfortunately, the cost of those benefit enhancements did not contemplate the unprecedented investment losses that followed, which have driven the cost of these benefits to a much higher level today.

City Administrator's Budget Message

In fiscal year 2013, the General Fund is expected to pay $16.3 million in pension contributions, representing 15.4% of the total General Fund budget. Over the next several years, employer contribution costs are expected to consume a larger portion of operating costs. This is based on two primary factors: (1) the current funding status of the City's plan which is currently between 60-63% funded; and (2) the anticipated medium-term outlook for investment performance.

The CalPERS Board recently lowered their assumed rate of return on its pension assets, which will result in increased employer rates starting in fiscal year 2014. This decision stemmed from an analysis of historical earnings, which over the last decade has not met the 7.75% target assumed by CalPERS.

CONCLUSION

The fiscal year 2013 recommended budget continues the City of Santa Barbara's slow recovery from the terrible recession that began nearly four years ago. Due to the early steps taken to reduce the size of the City organization, work with employees to reduce wage and benefit costs, and pay close attention to expense control, we have maintained the City's strong overall financial condition. We have also created a solid foundation to restore services and prepare for the future.

I am very proud of the efforts of our City organization to provide quality services to the community, even with less employees and resources. Through streamlined processes, new work procedures, and better use of technology, we have been able to maintain critical programs and carry out many important infrastructure projects.

I want to especially thank all of the employees who have been involved in preparing the fiscal year 2013 budget. It required countless hours of analysis, study and preparation. Especially important has been the cooperative attitude shown by the entire City management team to find creative solutions to minimize service impacts to our citizens.

I also want to recognize the amazing efforts of the City's strong financial management team led by Finance Director Bob Samario. Major contributors to this effort include Budget Manager Michael Pease, Treasury Manager Jill Taura, Accounting Manager Ruby Carrillo, Treasury Analyst Diego Martin, Budget Analyst Jonathan Abad, and Executive Assistant Jenny Hopwood. They often toiled late into the night to complete the final budget documents.

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Directory of City Officials

Helene Schneider
Mayor

Dale Francisco
Councilmember

Frank Hotchkiss
Councilmember

Grant House
Councilmember

Cathy Murillo
Councilmember

Randy Rowse
Councilmember

Harwood "Bendy" White
Councilmember

James L. Armstrong
City Administrator, City Clerk,
and City Treasurer

Stephen P. Wiley
City Attorney

Paul A. Casey
Assistant City Administrator

Marcelo A. Lopez
Assistant City Administrator

Karen S. Ramsdell
Airport Director

Robert Samario
Finance Director

Andrew Dimizio
Fire Chief

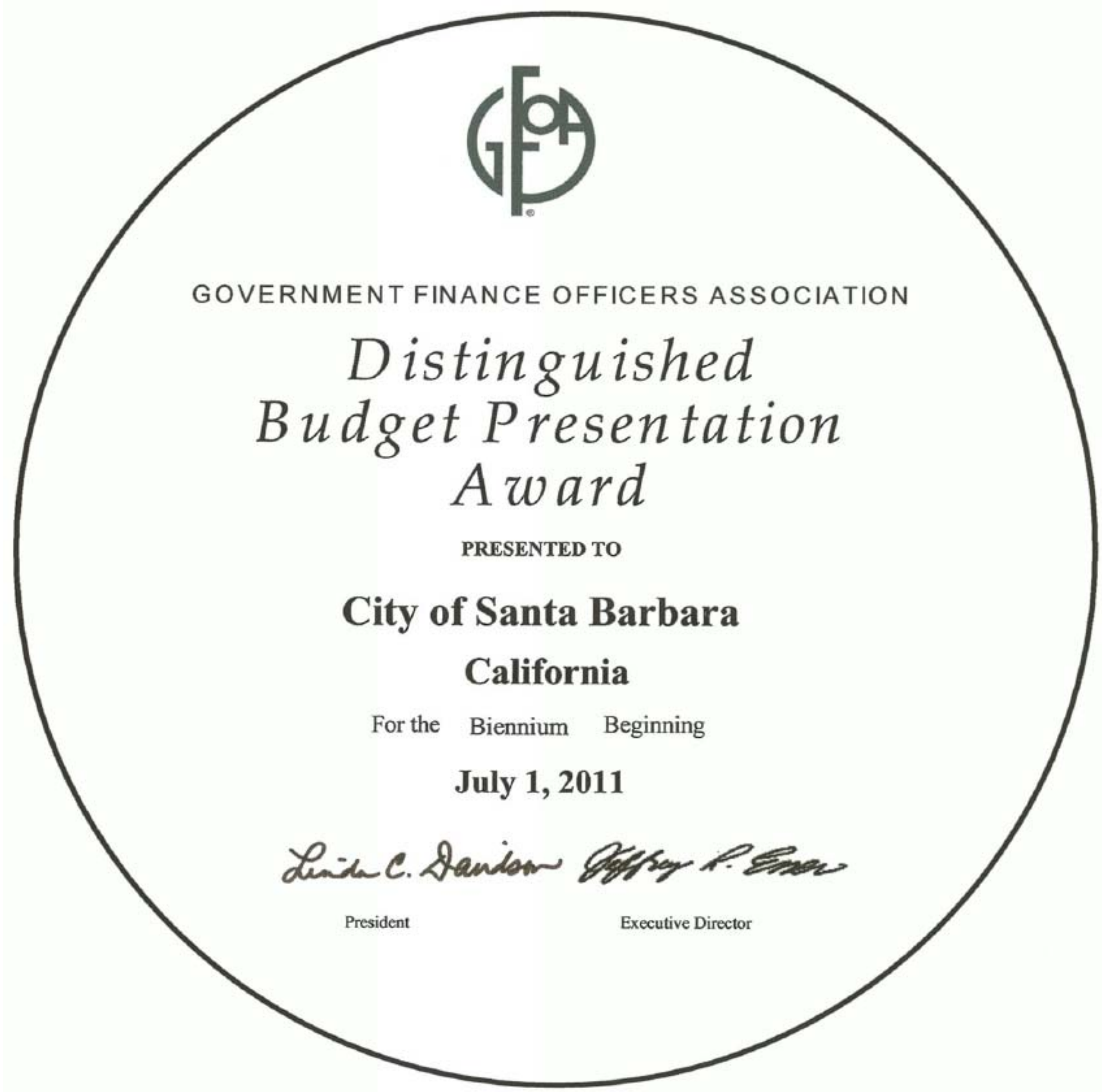
Irene Macias
Library Director

Nancy L. Rapp
Parks and Recreation Director

Camerino Sanchez
Police Chief

Christine Andersen
Public Works Director

Scott K. Riedman
Waterfront Director



GOVERNMENT FINANCE OFFICERS ASSOCIATION

Distinguished Budget Presentation Award

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The Government Finance Officers Association of the United States and Canada (GFOA) presented an award of Distinguished Presentation to City of Santa Barbara for its two-year financial plan and annual budget for the biennium beginning July 1, 2011 and ending June 30, 2013.

In order to receive this award, a governmental unit must publish a budget document that meets program criteria as a policy document, as an operations guide, as a financial plan, and as a communications device.

The award is valid for a period of two years, covering both years of the two-year plan. The mid-cycle budget is an addendum to the two-year plan and thus not submitted to GFOA for award consideration.